Model Guidelines for State Laws and Regulations

These guidelines are advisory in nature and set out general concepts rather than precise statutory language. The ICCFA is not recommending that the guidelines be codified into law as a whole. Instead, the guidelines are intended for consideration as a series of options to be selectively chosen by interested parties to address particular concerns.

Insurance-Funded Prearrangements

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Developed in 1998 by the Government and Legal Affairs Task Force of the International Cemetery and Funeral Association

BACKGROUND

The use of life insurance and annuity policies, as an alternative to other funding vehicles for prearrangements, has developed into a specialty market whereby these policies contain features which permit the death benefit of the life insurance policy to increase during the lifetime of the insured. These increases, whether indexed or discretionary, are designed to keep pace with the rising cost of providing pre-selected cemetery and funeral merchandise and services at some unknown time in the future.

These specialty policies contain all the standard features of life insurance and annuity products, but in addition, contain elements which are generally not readily available through the life insurance market. These are:

a. an increasing death benefit;
b. guaranteed issue;
c. issuance to the elderly;
d. issuance to those with impaired health.

Under a typical insurance-funded prearrangement, the consumer first prearranges for cemetery or funeral merchandise and services. It is this transaction which leads to the purchase of life insurance to fund the prearrangement. Generally, the initial face amount of the life insurance policy is based upon the current retail cost of the prearrangement. In many prearrangements, providers are willing to guarantee the price of some, or all, of the merchandise and services selected because of the feature in the life insurance policies whereby the death benefit increases over time.

To secure these guarantees, if any, and to facilitate payment of the prearrangement at time of death, the policy owner normally executes a contingent revocable assignment of the death benefit of the life insurance policy to the selected provider. It is important to note that the assignment is contingent upon actual fulfillment of the prearrangement by the provider. If no merchandise and services are provided, the precondition of the assignment does not occur, and death benefits are paid to the named beneficiary of the life insurance policy (normally a family member). During the lifetime of the insured, the policy remains transferable and the insured retains the right to change both the prearrangements and the freedom to choose a different provider.

Unlike prearrangements which are funded through prepaid contract trust funds, payment of premiums is NOT made to the provider. Instead, the consumer makes all payments directly to the life insurance company. Since no monies are exchanged for cemetery or funeral merchandise and services until after the consumer dies, there can be no "sale" of merchandise or services on a preneed basis subject to the state preneed laws.

The use of life insurance to pre-fund a prearrangement benefits the consumer in several ways. Single premium products always provide a death benefit greater in amount than the premium paid, thus for the same amount as would be placed into other funding, a greater initial amount of benefit is purchased. For those who cannot afford to pay a single premium, multiple payment plans provide two distinct advantages: a.) For those who can pass limited underwriting, full first day coverage is available. Since full benefits are available upon death (even when the total premium has not been paid), the provider is able to guarantee the prearrangement immediately. b.) For those who cannot pass the health questions, limited benefits are available during the first two years, but beginning the third year of coverage, full death benefits are available. Thus, the provider may guarantee the prearrangement at that time. In both scenarios, guaranteed prearrangements are available, whereas most other types of funding cannot provide guarantees until all payments are made. When payment schedules may extend over five to ten years, this is a considerable benefit to many consumers.

Finally, the nature of the life insurance market includes the payment of commissions. These commissions provide a source of income to sellers which permit them to pay current preneed expenses without tapping into other resources.

The National Association of Insurance Commissioners ("NAIC") has addressed the use of life insurance products in the funding of prearrangements, and adopted a model law which is designed to provide consumers with specified information when life insurance is selected as the funding source. In developing this model, the NAIC considered factors relevant to elderly consumers, in addition to standard disclosures to individuals purchasing life insurance products in this market.

PRINCIPLES

1. The NAIC model should be adopted substantially as follows, with the following information being disclosed at the time an application is made, prior to accepting the applicant's initial premium or deposit, for a prearrangement which is funded by a life insurance policy:
    a. The fact that a life insurance policy is involved or being used to fund a prearrangement;
    b. The nature of the relationship among the soliciting agent or agents, the provider of the merchandise or services, the administrator, and any other person;
    c. The relationship of the life insurance policy to the funding of the prearrangement and the nature and existence of any guarantees relating to the prearrangement;
    d. The impact of the prearrangement

- on any changes in the life insurance policy including, but not limited to, changes in the assignment, beneficiary designation or use of the proceeds;
- on any penalties to be incurred by the policy holder as a result of failure to make premium payments;
- on any penalties to be incurred or monies to be received as a result of cancellation or surrender of the life insurance policy;

e. A list of the merchandise and services which are applied or contracted for in the prearrangement and all relevant information concerning the price of the cemetery or funeral merchandise and services, including an indication that the purchase price is either guaranteed at the time of purchase or to be determined at the time of need;

f. All relevant information concerning what occurs and whether any entitlements or obligations arise if there is a difference between the proceeds of the life insurance policy and the amount actually needed to fund the prearrangement;

g. Any penalties or restrictions, including but not limited to, geographic restrictions or the inability of the provider to perform, on the delivery of merchandise, services, or the prearrangement guarantee;

2. Since dual regulation of prearrangements funded through life insurance does occur, it is important that laws concerning the prearrangement process do not overlap into the regulation of the life insurance product itself.

3. Reporting of transactions funded with life insurance should be designed specifically for life insurance and not based upon the same criteria as prepaid contract trust funds. The impact of graded death benefits, increases in death benefit which are not related to "interest," lapses, and surrenders have no relevance to prepaid contract trust fund reporting requirements. Since life insurance company transactions are regulated and audited separately, there should be no additional requirements imposed by the regulatory authority that oversees prepaid contract trust funds.

4. Medicaid and Supplemental Security Income benefits eligibility may have an impact upon individuals who fund their prearrangement with life insurance. The use of the irrevocable assignment of ownership, either to the provider or into a life insurance trust, should be available in order to protect the eligibility rights of this class of consumers.

5. In the event that a life insurance company participates in an insurance guarantee association, there should be no requirement for a separate contribution to a consumer guarantee fund for prepaid contracts.

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